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No. 95-1402

In the Supreme Court of the United States

OCTOBER TERM, 1995

COMMISSIONER OF INTERNAL REVENUE, PETITIONER

v.

ESTATE OF OTIS C. HUBERT, DECEASED,
C & S SOVERAN TRUST COMPANY (GEORGIA) N.A.,
A NATIONAL BANKING ASSOCIATION, CO-EXECUTOR

ON WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE ELEVENTH CIRCUIT

REPLY BRIEF FOR THE PETITIONER

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Sections 2055 and 2056 of the Internal Revenue Code provide a marital and charitable deduction equal to the "value" at the date of death of property that passes to a surviving spouse or charity. When a marital or charitable bequest is burdened by the obligation of paying the expenses of administration of the estate, those costs—whether paid directly from the corpus or from the post-death income earned by the corpus of the bequest—must be subtracted from the gross value of the bequest in determining the "net value" or "real value of the gift" (*United States* v. *Stapf*, 375 U.S. 118, 125, 126 (1963)). As our opening brief describes in detail, the text and history of Sections 2055 and 2056, the contemporaneous regulations

of the Treasury Department and the decisions of this Court and of all but one of the courts of appeals require this same conclusion. See Pet. Br. 20-29; *Burke* v. *United States*, 994 F.2d 1576, 1581-1582 (Fed. Cir.), cert. denied, 114 S. Ct. 546 (1993); *Estate of Street* v. *Commissioner*, 974 F.2d 723, 726 (6th Cir. 1992); *Estate of Roney* v. *Commissioner*, 294 F.2d 774 (5th Cir. 1961), aff'g per curiam 33 T.C. 801 (1960).

None of the contrary arguments advanced by respondents withstands scrutiny. As the Fifth Circuit stated in *Alston* v. *United States*, 349 F.2d 87, 89 (1965):

> No amount of legalistic legerdemain can produce * * * "the principle that where expenses of administration are paid out of post-mortem income, the amount of corpus available for charity is not diminished by such payments * * * " as argued by the executors.

1. Respondents err in suggesting that the Commissioner's longstanding interpretation of Sections 2055 and 2056 yields "startling" (Resp. Br. 34) tax consequences. As the following example reveals, it is the position advanced by respondents that would produce irrational results.

Assume that a gross estate of $2,000,000 is left entirely to a surviving spouse, that the estate incurs and pays $500,000 in administration expenses and that the estate has income of $500,000 during the period of administration:[1]

> (I) If the estate pays the administration expenses out of the corpus of the bequest, it is

[1] For ease of exposition, these examples ignore the $600,000 unified credit provided by 26 U.S.C. 2010. If that credit were taken into account, it would complicate the discussion but not alter its substance.

undisputed (Pet. Br. 9; Resp. Br. 6, 18) that the estate has an administration expense deduction of $500,000 (under Section 2053(a)) and that the marital deduction is reduced by the amount of these administration expenses to $1,500,000 ($2,000,000 less $500,000). In this scenario, the estate has no *estate* tax liability because its total deductions still equal $2,000,000. The estate would be required, however, to pay *income* tax on its income of $500,000.

(II) If, however, the estate (as in the present case) pays the administration expenses out of its post-death income and elects under Section 642(g) of the Code to deduct those expenses on its *income* tax return rather than on its *estate* tax return, the analysis of the parties reaches different results.

> (i) Under the established view of the Commissioner, the election by the estate to take the deduction for administration expenses on its income tax return is effective to eliminate the *income* tax liability of the estate because the income of the estate and the deduction claimed under Section 642(g) are both $500,000 in this example. But the estate is then subject to the *estate* tax on a net estate of $500,000 because, as in example (I), the marital deduction must be reduced to $1,500,000 (due to the fact that the marital interest is burdened by the obligation to pay administration expenses) but, unlike in example (I), there is no administration expense deduction on the *estate* tax return because the estate elected to take that deduction on its income tax return. A taxable estate of $500,000 results in this example, but no income tax liability exists.

(ii) Under the construction of these provisions urged by respondents, however, the estate would escape *both* income and estate taxation for the entire bequest *and* for the post-death income of that bequest simply by electing to apply income, rather than corpus, to pay the administration expenses. In respondents' view, the marital deduction would be $2,000,000 (and would thus eliminate the estate tax) and the administration expense deduction elected under Section 642(g) on the estate's *income* tax return would eliminate its income tax liability.

For the reasons explained in detail in our opening brief (Pet. Br. 20-22), Congress did not enact these provisions to provide an elective tax shelter that would permit the estate to avoid all taxes on *both* corpus and income, as respondents implicitly contend. Instead, as the case law and the Commissioner's longstanding interpretation reflect, the estate either (i) may elect to take the administration expense deduction against the *estate* tax, leaving its post-death income subject to income tax, or (ii) may elect to take that deduction against its *income* tax, leaving that same portion of the estate subject to the estate tax. Section 642(g) provides an election for the application of this deduction, not a tax avoidance mechanism as respondents contend. See pages 17-18, *infra*.

2. Contrary to the contention of respondents and the amici, an obligation to pay administration expenses is not different in substance from an obligation to pay estate taxes or an obligation to pay any other burden or encumbrance imposed on a marital or charitable bequest. All such obligations reduce the "real value" or "net value" of the marital and charitable bequests in precisely the same manner.

a. Sections 2055 and 2056 expressly require that, when the burden of paying estate taxes is placed on the marital or charitable bequest, the marital or charitable deduction is to be "reduced by the amount of such taxes" (26 U.S.C. 2055(c); see 26 U.S.C. 2056(b)(4)(A)). This reduction is required without regard to whether these expenses are paid from estate corpus or estate income.

As explained in detail in our opening brief (Pet. Br. 20-22), Section 2056(b)(4)(B) articulates this same principle in a broader context. It provides that, when a marital bequest "is encumbered *in any manner*, or where the surviving spouse incurs *any obligation* imposed by the decedent with respect to the passing of such interest, such encumbrance or obligation shall be taken into account" in computing the amount of the marital deduction. 26 U.S.C. 2056(b)(4)(B) (emphasis added). As with estate taxes under Section 2056 (b)(4)(A), the encumbrances and obligations referred to in Section 2056(b)(4)(B) must be subtracted from the marital deduction without regard to whether they are paid from estate corpus or from estate income. As the legislative history of that provision explains, if the decedent bequeaths the residuary interest to the surviving spouse "and she pays, *or if estate income is used to pay*, claims against the estate so as to increase the residue, * * * the value of any such additional part of the residue passing to the surviving spouse can not be included in the amount of the marital deduction." S. Rep. No. 1013, 80th Cong., 2d Sess., Pt. 2, at 6 (1948) (emphasis added).

b. The broad language that Congress employed in Section 2056(b)(4)(B) is obviously comprehensive, rather than restrictive, in scope. The statute applies to "any manner" of encumbrance and "any obligation" imposed on a marital bequest. 26 U.S.C.

2056(b)(4)(B).[2] Administration expenses like estate taxes, mortgages and other burdens on a marital or charitable bequest—are an "encumbrance" or "obligation" within the scope of this statute because (i) the estate cannot be transferred to the beneficiary without incurring and paying those expenses and (ii) the burden of those expenses reduces the "real value" of the bequest (*United States* v. *Stapf*, 375 U.S. at 126).[3]

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[2] Congress did not limit the coverage of Section 2056(b)(4)(B) to mortgages, as the Florida Bar (Fl. Bar Amicus Br. 14) contends. While mortgages are listed in the legislative history as one example of an encumbrance or obligation placed on a bequest (S. Rep. No. 1013, *supra*, Pt. 2, at 6), an example of the application of a statute contained in its legislative history does not restrict the meaning of the statute (*United States* v. *National City Lines*, 337 U.S. 78, 81 (1949)):

> Obviously, an example is not a complete catalogue. The use of an example implies no purpose to restrict the meaning of the statutory phrase * * * precisely to the illustration selected.

[3] The basic principle of Section 2056(b)(4)(B)—that the marital deduction must be reduced by the amount of encumbrances that burden that bequest—is not limited to the marital deduction. In enacting this provision, Congress noted that the principles it embodies are "generally applicable in determining the net value of *any* gift or bequest." S. Rep. No. 1013, *supra*, Pt. 2, at 6 (emphasis added). The courts have thus consistently and correctly applied the marital and charitable provisions of the estate tax in *pari materia*, construing them in a consistent fashion. See, *e.g.*, *Burke* v. *United States*, 994 F.2d 1576 (Fed. Cir.), cert. denied, 510 U.S. 990 (1993) (charitable deduction); *Alston* v. *United States*, *supra* (charitable deduction); *Estate of Street* v. *Commissioner*, 974 F.2d 723 (6th Cir. 1992) (marital deduction); *Ballantine* v. *Tomlinson*, 293 F.2d 311 (5th Cir. 1961) (marital deduction). As one of the amici concedes, although Section 2055 does not contain an express provision corresponding to Section 2056(b)(4)(B), "from a conceptual standpoint the same limitations should apply" (Fl. Bar Amicus Br. 24).

As this Court explained in *Stapf*, "administration expenses" are like other claims against the estate because, with respect to both, the testator, "by directing that payment be made of debts chargeable to another or to non-estate property, *reduces his net estate and in effect confers a gift or bequest upon another.*" *Id.* at 134 (emphasis added).

As *Stapf* indicates, reducing the marital or charitable deduction by the amount of the burdens imposed on those bequests does not—as respondents suggest—cause a portion of the estate to "disappear" (Resp. Br. 13). When the obligation to pay administration expenses is imposed on the marital or charitable bequest, that "reduces [the] net estate" attributable to that bequest by "in effect" conferring that portion of the "bequest upon another" (375 U.S. at 134). Because that portion of the bequest has, "in effect," been allocated for the payment of administration expenses—rather than to the marital and charitable beneficiaries—the marital and charitable deductions are reduced commensurately. See *id.* at 125-126.

c. The fact that administration expenses are incurred after death does not distinguish them from other burdens that reduce the marital and charitable deductions. See Pet. Br. 24-25; *Ballantine* v. *Tomlinson*, 293 F.2d at 312-313.

Like administration expenses, estate taxes also do not come into existence and cannot be calculated until after death. But Congress expressly provided that the marital and charitable deductions are to be reduced by the amount of such taxes. 26 U.S.C. 2055(c), 2056(b)(4)(B). Moreover, respondents concede (Resp. Br. 6, 18) that, when administration expenses are paid from the corpus of the estate, the marital and

charitable deductions must be reduced by the amount of these expenses. Administration expenses paid from estate corpus are not different in nature from administration expenses paid from estate income—both come into existence after the decedent's death and both operate to reduce the value of the bequest and therefore to reduce the amount of the marital and charitable deductions.[4]

Respondents nonetheless object to this application of the statute for requiring what they describe as a "hindsight approach to valuation" (Resp. Br. 20). In *Harrison* v. *Northern Trust Co.*, 317 U.S. 476 (1943), however, the Court explained that Congress has expressly required such "hindsight" calculations to be made in valuing the marital and charitable deductions. As the Court stated in that case, the objection to the "fact that the tax may have to be computed by an algebraic formula or by complicated arithmetical methods * * * loses all significance when it is remembered that" the statute imposes this requirement. *Id.* at 481.

3. Respondents and the amici virtually ignore the decision of this Court in *United States* v. *Stapf*, 375 U.S. 118 (1963). Only one of the four amici even acknowledges its existence (Fl. Bar Amcius Br. 11) and, although respondents refer to this decision, they do so only in an effort to limit it to its facts. Respon-

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[4] In *Estate of Street* v. *Commissioner*, 974 F.2d 723 (6th Cir. 1992), the court of appeals concluded that, unlike administration expenses, payments of interest due on estate taxes do not reduce the marital deduction. Although courts have differed as to whether interest is a deductible administration expense (see *Estate of Whittle* v. *Commissioner*, 994 F.2d 379, 382-384 (7th Cir. 1993) (citing cases)), the Commissioner has acquiesced in the ruling in *Estate of Street* (Rev. Rul. 93-48, 1993-2 C.B. 270).

dents claim that *Stapf* is "a *quid pro quo* case" that applies only when the surving spouse is required to make a payment from her own funds as a condition of receiving the marital bequest (Resp. Br. 34). This attempt to narrow the holding of *Stapf* ignores the text of the decision and the text of the statute.

The statute involved in *Stapf*—Section 2056(b)(4)(B)—requires a reduction of the marital deduction when the marital interest is burdened by *any* encumbrance or obligation, not merely by a "quid pro quo." See pages 5-6, *supra*. The Court explained in *Stapf* that, under this statute, "[t]he appropriate reference" in determining the marital deduction "is not to the value of the gift moving from the deceased spouse but the net value of the gift received by the surviving spouse" (375 U.S. at 125). The Court stated that, when the marital bequest is burdened by the requirement that it be used to pay obligations of the estate, "the real value of the gift" is only "the net economic interest received by the surviving spouse" (*id.* at 126), which is the gross value of the gift reduced by the cost of satisfying the obligations imposed on the bequest. *Ibid.*[5]

Respondents' attempt to narrow *Stapf* to its facts is transparently an effort to avoid this clear holding of *Stapf*. For the reasons described in our opening brief (Pet. Br. 20-24), the holding in *Stapf* applies to, and governs, the present case.

4. Respondents and the amici misconstrue the meaning of the portion of Section 2056(b)(4)(B) that states that any "encumbrance or obligation" on the

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[5] Respondents suggest that the Commissioner has improperly "extract[ed]" a "'real value' principle * * * from *Stapf*" (Resp. Br. 34). But that principle did not have to be "extract[ed]" from *Stapf*—it was the express *ratio decidendi* of the holding in that case. 375 U.S. at 126.

marital bequest is to "be taken into account in the same manner as if the amount of a gift to such spouse of such interest were being determined." 26 U.S.C. 2056(b)(4)(B). They erroneously contend that this statutory directive incorporates various gift and estate tax regulations and revenue rulings (Resp. Br. 37-41; Amer. Coll. Tr & Est. Amicus Br. 10-11; Coun. Ed. Amicus Br. 13-14).

The regulations and rulings that they cite, however, do not deal with the *amount* of the marital and charitable deductions, which is the issue addressed in this case. Instead, these regulations and rulings address the threshold question of the estate's *eligibility* for a marital deduction. A gift or bequest is *eligible* for the marital deduction only if the property involved is transferred to the spouse both in form and in substance. The Treasury Regulations list several conditions that must be met for the marital deduction to be available for a transfer in trust. One of these conditions is that the surviving or donee spouse must be entitled for life to all of the income from the entire interest. 26 C.F.R. 20-2056(b)-5(f), 25.2523(e)-1(a)(1). Certain powers vested in the trustee that may constrain the spouse's right to receive income, however, will nonetheless "not have the effect of disqualifying an interest transferred in trust" (26 C.F.R. 25.2523(e)- 1(f)(4)). One of those is "the power to determine the allocation or apportionment of receipts and disbursements between income and principal." *Ibid.*; see also 26 C.F.R. 20.2056(b)-5(f)(4). These regulations address only whether the mere existence of such a power in the trustee will "disqualif[y]" the transfer from the marital deduction. That is a far different question from the question presented in this case, which is the effect that the *exercise* of such a power may have on the *amount* of the marital deduction. These regulations do not purport to deal with

the latter question, as respondents and amici only indirectly acknowledge.[6]

The Revenue Ruling cited by respondents (Rev. Rul. 69-56, 1969-1 C.B. 23) is similarly inapposite. That Ruling describes various powers that may be granted to the trustee of a marital trust—including the power of the fiduciary to charge expenses of administration either to income or principal—and states that the "inclusion of such powers or directions in the governing instrument" and "the grant of such power in and of itself" will not result in the denial or diminution of the marital deduction. 1969-1 C.B. at 224, 225. This Ruling, like the regulations

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[6] Respondents briefly note that the regulations that they cite establish the requirements for "a gift in trust to a spouse [to] *qualify* for a gift-tax-free transfer" and list the permissible powers of the trustee that, even though they may interfere with the spouse's free enjoyment of the gift, will not cause the "marital deduction [to] be *disqualified*" (Resp. Br. 38, 39 (emphasis supplied)). The amici are equally indirect in describing these regulations. For example, while amici American Council on Education and United Way purport to rely extensively on "[t]he relevant gift tax regulations," they acknowledge that the regulations only state the rules that apply in determining whether "a trust will *qualify* for the marital deduction" (Amer. Coun. et al. Amicus Br. 13). The regulations cited by respondents and amici deal with "qualification," not with "valuation." This case, by contrast, concerns the proper "valuation" of an unquestionably "qualified" bequest.

Because these regulations do not deal with the valuation of the marital deduction, there is no merit to the contention of the amicus American College of Trust and Estate Counsel (Amer. Coll. Tr. & Est. Amicus Br. 10-12) that the Commissioner's position creates inconsistent tax treatment of estates governed by wills and those governed by revocable trusts.

that it interprets,[7] does not address the question of how the *exercise* of such powers may affect the proper valuation of a qualified marital deduction.[8]

The applicable "valuation" regulation is 26 C.F.R. 20.2056(b)-4(a), which was adopted contemporaneously with Section 2056(b)(4)(B) of the Code.[9] That regulation specifies that the amount of any encumbrance or obligation imposed on a marital bequest (including the burden of paying administration expenses) is to be subtracted from the gross value of that bequest in determining the marital deduction under Section 2056, just as it would be in valuing a gift for gift tax purposes (see Stephens, Maxfield, Lind & Calfee,

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[7] This Ruling interprets the regulations that describe the type of income interest that the spouse must receive for the transfer to *qualify* for a marital deduction. 26 C.F.R. 20.2056(b)-5(f)(1)-(4), 25.2523(e)-1(f)(4). Under these regulations, for the marital deduction to apply, the surviving spouse must have substantially that degree of beneficial enjoyment of the trust that would be afforded to a life beneficiary of a trust.

[8] The fallacy in respondents' invocation of the revenue ruling and regulations that relate to the *qualification* of the marital interest for the marital deduction is manifest. It would follow from their reading of these regulatory provisions that a reduction in the marital deduction would not be required even when administration expenses are paid from the corpus of the estate—a contention that no party has advanced and no court has accepted.

[9] Respondents acknowledge that this case turns on "valuation," for the ultimate issue is the proper "value" of the marital and charitable bequests (26 U.S.C. 2055(a), 2056(a)). Respondents err, however, in stating that "valuation" is a purely factual question (Resp. Br. 16, 46). The question presented is a legal one, not a factual one. It is whether, as the Commissioner submits, the "value" of the marital and charitable bequests is reduced by the burden imposed on those bequests to pay the expenses of admininstration of the estate.

Federal Estate and Gift Taxation ¶ 10.21[2][a] n.24 (6th ed. 1991), quoting S. Rep. No. 1013, *supra*, Pt. 2, at 6; *Laughinghouse* v. *Commissioner*, 80 T.C. 425, 430 (1983); *Drybrough* v. *United States*, 208 F. Supp. 279, 283 (W.D. Ky. 1962)). The regulation also makes it clear that this reduction is required whether the burden is satisfied through distributions of corpus or of "the income from the property" (26 C.F.R. 20.2056(b)-4(a)). The regulation thus implements the express understanding of Congress that, when the spouse pays directly, or "estate income is used to pay, claims against the estate," the marital deduction is reduced by the amount of such payments. S. Rep. No. 1013, *supra*, Pt. 2, at 6.[10]

Section 20.2056(b)-4(a) of the regulations broadly provides that any "material limitation" on the right of a spouse to receive income earned by the corpus of the marital bequest reduces the "value" of that bequest and therefore commensurately reduces the marital deduction. 26 C.F.R. 20.2056(B)-4(A). The burden of paying administration expenses constitutes a "material" limitation on the right of the surviving spouse to receive income within the meaning of this regulation, for it "reduces [the] net estate and in effect confers a gift or bequest upon another" (*United States* v. *Stapf*, 375 U.S. at 134). As the text of the regulation directly notes (*ibid.*):[11]

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[10] As Judge Dubina noted (Pet. App. 22a), and as the Fifth Circuit held in *Ballantine* v. *Tomlinson*, 293 F.2d at 313, the reference to "claims" in the legislative history is equally applicable to administration expenses. "The reason for including the one applies to the other." *Ibid.* See also *United States* v. *Stapf*, 375 U.S. at 134; pages 6-7, *supra*.

[11] The court of appeals noted that the administration expenses in this case were "over $2,000,000" (Pet. App. 3a). Although respondents suggest that some smaller amount was

> An example of a case in which this rule may be applied is a bequest of property in trust for the benefit of the decedent's spouse but the income from the property * * * is to be used to pay expenses incurred in the administration of the estate.

5. Federal law, not state law, governs the resolution of this case. State law is relevant in determining the amount of allowable administration expenses and in determining whether such expenses are allocated to income or corpus. See Rev. Rul. 69-193, 1969-1 C.B. 222. As we explain in detail in our opening brief (Pet. Br. 31-33), however, federal law—not state law— determines the consequences that such expenses have in calculating the marital and charitable deductions on the federal estate tax return.[12]

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actually incurred (Resp. Br. 5 n.3), the record amply supports the court's calculation. The estate deducted administration expenses of $500,000 on the estate tax return and of $1,458,445 on the estate's income tax returns for the period between May 31, 1987, and May 31, 1990 alone (C.A. App. 53). See also C.A. App. 34-36, 42-43.

[12] Amici err in contending (Amer. Coun. Ed. Amicus Br. 9) that *Riggs* v. *Del Drago*, 317 U.S. 95 (1942), is to the contrary. That case did not involve the imposition of the federal estate tax. It involved the allocation—under the decedent's will and under state law—of the burden of that tax among the beneficiaries of the estate. *Harrison* v. *Northern Trust Co.*, 317 U.S. 476 (1943), which amici also cite, also involved the application of state law in determining the allocation of the estate tax "among the beneficiaries" (Amer. Coun. Educ. Amicus Br. 9). But that "state law" question has no relevance to this case. The administration expenses involved in this case were unquestionably allocated, under the will and under state law, to the marital and charitable bequests. The question that remains to be resolved—the proper construction of Sections 2055 and 2056 of the Internal Revenue Code—is purely a question of federal law.

There is no merit to respondents' contention that the Commissioner "dance[s] to a new tune" (Resp. Br. 29) in arguing that federal law controls this issue. The Commissioner's position in this litigation is far from new. For example, in the appellate brief filed by the government in 1961 in *Ballantine* v. *Tomlinson*, *supra*, the government argued that, "[u]nder federal law, a residuary bequest to a spouse must be reduced by the portion of administration expenses chargeable against it, regardless of the source from which they are actually paid" (Gov't C.A. Br. at 18 (No. 18,736)). Similarly, in 1965 in *Alston* v. *United States*, *supra*, the government argued alternatively (i) that the executors lacked power under state law to charge administration expenses to post-mortem income and (ii) that, if the executors had such power under Georgia law, federal law nonetheless required the charitable deduction to be reduced by the amount of administration expenses without regard to whether those expenses were paid from corpus or income.[13] The Commissioner took the same position in *Estate of Roney* v. *Commissioner*, 294 F.2d 774 (5th Cir. 1961).[14]

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[13] The brief filed by the United States in that case stated (Gov't C.A. Br. at 15 (No. 21,492)):

> [E]ven if, *arguendo*, the executors had the power under Georgia law to pay the administration expenses out of post-mortem income (which we deny), it nevertheless appears clear from reading Sections 2053, 2055 and 2056 of the 1954 Code * * * that the value of a gift of the residuum to a charity and the size of a charitable deduction which affects the statutory taxable estate should correspondingly also reflect a diminution of value of such residuum by the amount of the administration expenses * * *.

[14] In *Estate of Warren* v. *Commissioner*, 981 F.2d 776 (5th Cir. 1993), the government relied solely on the terms of the

Prior to the decision in the present case, the courts of appeals had consistently agreed with the Commissioner that, although state law determines whether administration expenses are to be paid from corpus or from the income attributable to the corpus, either type of payment reduces the "value" of the marital bequest and therefore reduces the marital deduction as a matter of federal law.[15] For example, in *Burke* v. *United States*, 994 F.2d at 1581, the court held that "[a]though [S]ection 2053 permits state law to determine what administrative expenses are 'allowable,' how section 2053 treats the allowable administrative expenses for estate tax deduction purposes is a federal question." See also *Estate of Street* v. *Commissioner*, 974 F.2d at 728; *Alston* v. *Commissioner*, 349 F.2d at 89 ("The effect of yielding to the executors' argument here would be to increase the amount of the gross estate by the amount of post-mortem income—a result directly contrary to the statutory definition of the gross estate."); *Estate of Roney* v. *Commissioner*, 33 T.C. at 803.

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will, which explicitly provided that all administration expenses were to be deducted from the corpus of the residuary estate. The government did not, as it customarily has done, alternatively address the ultimately controlling issue of federal law. See note 13, *supra*. That failure appears traceable to what (in retrospect) appears to have been a miscalculation of the strength of the government's position under the express terms of the will. It does not reflect any change in the Commissioner's longstanding view that, under federal law, any burdens on marital or charitable bequests reduce the value of those bequests (and therefore reduce the permissible marital and charitable deductions) without regard to whether the burden is paid from corpus or income.

[15] Commentators also have supported the Commissioner's consistent interpretation on this issue. See, *e.g.*, Gans, *Will Administration Expenses Charged to Income Reduce the Marital Deduction?*, 71 Journal of Taxation 90, 91 (August 1989); Brogan and Painter, *Administration Expenses May Lower Other Deductions*, 21 Estate Planning 131, 136, 137 (May/June 1994); Irwin, *Tax Law: Administrative Expenses and the Charitable and Marital Deduction—the Potentially Painful Surprise of a 642(g) Election—Estate of Hubert v. Commissioner*, 20 U. Dayton L. Rev. 501 (1994). See also Pet. App. 77a (Beghe, J., dissenting).

Respondents also cite various revenue rulings (Resp. Br. 29) in arguing that the Commissioner is now "danc[ing] to a new tune." These rulings, however, refer to state law only in determining the allowability of administration expenses, not in determining the federal tax consequences of allowable expenses. For example, in Rev. Rul. 66-21, 1966-1 C.B. 219, modified, Rev. Rul. 69-193, *supra*, the Treasury ruled that the deductibility of administration and funeral expenses of an estate subject to Texas community property laws depended on whether, under Texas law, all of the expenses, or only one-half, were chargeable to the decedent. Similarly, in Rev. Rul. 88-12, 1988-1 C.B. 330, and Rev. Rul. 78-419, 1978-2 C.B. 244, rendered obsolete by Rev. Rul. 88-12, *supra*, the Treasury ruled that whether administration expenses were to be paid from property passing to the surviving spouse or to other beneficiaries is to be determined under the will and state law. In the present case, by contrast, it is undisputed (i) that the administration expenses were allowable as a matter of state law and (ii) that the maritable and charitable bequests, and not any other beneficiary, were burdened by the obligation of paying those expenses. The revenue rulings cited by respondents thus simply have no relevance to this case.

6. The Florida Bar errs in contending (Fl. Bar Amicus Br. 3, 26-29) that the Commissioner's position will force all estates to account for administration expenses on their estate tax returns rather than on

their income tax returns, and will thereby make ineffective the election provided by Section 642(g) of the Internal Revenue Code. That statute, which was enacted in 1942, permits estates to deduct administration expenses on their income tax return (as expenses of producing income under 26 U.S.C. 212) *only* if they file a written waiver of their right to deduct such expenses on their estate tax return (as expenses of administration of the estate under 26 U.S.C. 2053(a)). 26 U.S.C. 642(g). The statute thus ensures that estates do not claim a deduction for these expenses on *both* returns. *Ibid.* See H.R. Rep. No. 2333, 77th Cong., 1st Sess. 75-76 (1942).

By thus prohibiting a double deduction of administration expenses, Congress did not ensure taxpayers that they would always benefit from the election that they make. Nothing in Section 642(g) seeks to alter the tax consequences of the deduction of such expenses under the substantive provisions of the estate tax and income tax. The statute is therefore not relevant to the proper interpretation of the substantive estate and income tax provisions involved in this case. See, *e.g.*, *Estate of Luehrmann* v. *Commissioner*, 287 F.2d 10, 12-13 (8th Cir. 1961); *Estate of Roney*, 33 T.C. at 804.[16]

Moreover, it is simply incorrect to suggest that, under the Commissioner's position in this case, estates would not be able to benefit from the election permitted by Section 642(g). The vast majority of estates—those that are not subject to the estate tax

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[16] The marital deduction did not even exist at the time Section 642(g) was enacted and there is no reference in the legislative history of Section 642(g) to the computation of the charitable deduction. S. Rep. No. 1631, 77th Cong., 2d Sess. 136 (1942); H.R. Conf. Rep. No. 2586, 77th Cong., 2d Sess. 52 (1942).

because of the $600,000 unified credit—will continue to benefit by deducting administration expenses on their income tax return. Without the election permitted by Section 642(g), these estates would obtain no benefit from administration expense deductions.[17] See J. Pennell, 239-4th *Tax Management Portfolio* (BNA) at A-22. Moreover, even when an estate is subject to tax, the estate will benefit from deducting administration expenses on its income tax return when the marginal tax bracket for income tax purposes exceeds the applicable bracket for estate tax purposes. These two types of estates are the dominant majority, not the exception.[18]

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[17] Other circumstances can also cause an estate not to be subject to the estate tax. For example, if the decedent leaves all his property to his surviving spouse or to charity, the estate will have no estate tax liability if it pays all administration expenses from corpus (Pet. Br. 9). Moreover, even if the estate pays administration expenses from income, it will incur no estate tax liability if the entire estate is bequeathed to the surviving spouse or charity and the administration expenses do not exceed the unified credit of $600,000.

[18] For reasons previously stated in detail (Pet. Reply Br. on Petition for Writ of Certiorari 5-6), there is no merit to respondents' suggestion (Resp. Br. 7-8, 48-49) that a decision on the legal issue presented in this case will have no effect on the estate's tax liability. The Commissioner has performed a tentative recalculation of the estate tax liability based on the assumption that the marital and charitable deductions are to be reduced by the administration expenses that had been deducted on the estate's income tax returns for the period prior to September 26, 1991 ($1,656,859). That calculation, which is based upon the parties' computations for the entry of decision in the Tax Court (Pet. App. 65a-73a), was submitted to the court of appeals and was attached as an appendix to the reply brief in support of the certiorari petition. Under this calculation, a reversal in this case would result in (i) elimination of the

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For the foregoing reasons and those stated in our opening brief, the judgment of the court of appeals should be reversed.

Respectfully submitted.

WALTER DELLINGER
Acting Solicitor General

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overpayment of $344,438 determined by the Tax Court and (ii) an additional liability for the estate for an estate tax deficiency in excess of $154,000.